COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS & ENERGY

Petition of Boston Gas Company d/b/a KeySpan Energy Delivery New England, pursuant to General Laws Chapter 164, § 94, and 220 C.M.R. §§ 5.00 et seq. for a general increase in gas rates.

D.T.E. 03-40

REPLY BRIEF OF THE MASSACHUSETTS OILHEAT COUNCIL, INC. AND THE MASSACHUSETTS ALLIANCE FOR FAIR COMPETITION, INC.

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Dated: September 16, 2003
Albany, New York

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I. INTRODUCTION

This reply brief is filed on behalf of the Massachusetts Oilheat Council, Inc. (MOC) and the Massachusetts Alliance for Fair Competition, Inc. (Alliance) in accordance with the procedural schedule and orders established by the Department of Telecommunications and Energy (Department) in this proceeding. MOC and the Alliance (collectively referred to as "intervenors") submit this reply brief in response to the answering brief of the Boston Gas Company d/b/a KeySpan Energy Delivery New England ("Boston Gas", "Company" or "Utility").

The intervenors reply to the points raised by the Company in its initial brief pertaining to the Company's non-advertising promotional expenses, the Company's promotional advertising expenses, the intervenors' request for a payback analysis and the intervenors' request for a name change of KeySpan affiliates of the Company that perform HVAC services within the Boston Gas territory.[1]

II. ARGUMENT

A. THE COMPANY'S NON-ADVERTISING PROMOTIONAL EXPENSES SHOULD BE REJECTED

In its initial brief, the intervenors asked that the Department's review of the Company's proposed promotional expenses take into account the current state of the natural gas industry. (Intervenors' Br. pt. IV.B.1.). The intervenors believe that the potential for price impacts upon new customers and the Company should be considered before approving the requested promotional expenses such as the free equipment program designed to entice customers to convert to natural gas. MOC and the Alliance also requested that promotional programs offering potential customers free equipment or rebates include a statement warning the customers of potential price increases. The Company responds that there exists no Department standard requiring the Company to demonstrate "that the price of its product compares favorably to historic prices or even prices for other fuels" in order for the promotional expenses to qualify for a rate recovery (Company Br. p. 93).

The intervenors have not claimed that Department precedent requires a utility to

[1] The Company did not address intervenor MOC's request for interruptible customers to have adequate standby backup fuel.

demonstrate that the price of its product compares favorably to historic prices or to other competing fuels. Instead, MOC and the Alliance believe that the serious supply and price concerns of natural gas, as expressed by industry, government and political leaders, should be considered when determining the appropriateness of the Company's promotional expenses. As explained in the intervenors' initial brief, these promotional programs are luring customers - - with promises of free equipment, rebates, and a full satisfaction guarantee - - to convert to natural gas when it may be uneconomical for the customer to do so. In exercising its mandate to act in the public interest, it is both logical and reasonable for the Department to inquire whether it is prudent for the Company to invest ratepayer funds in such promotional programs at this time.

The Company also states that its justification for recovery of promotional expenses need not include a demonstration of direct benefits to ratepayers (Company Br. p. 93). The intervenors urge the Department to examine both direct benefits and net benefits of the promotional expenses.

The Department's cases indicate that for promotional expenses that do not fall within the specific statutory exemption, the utility must demonstrate that the promotion directly benefit ratepayers in order to be recoverable. (See, for example, Boston Gas D.P.U. 93-60 [1993]). Therefore the intervenors believe that a two-step review approach is necessary to assure that ratepayers are receiving both direct and net benefits from the inclusion of these promotional expenses within the cost of service. Failure to include a direct benefit test would result in the inclusion of programs that are remote and promote little or no benefit to the existing ratepayer.

With regard to the net benefits review, the Company contends that it has met this test by its IRR calculation (Ex. D.T.E. 4-28).[2] The intervenors believe that the Company's IRR approach is inconsistent with Department precedent, permits the inclusion of ineffective programs and unrecoverable expenses, and is not properly calculated.

The Company's aggregate approach does not satisfy the net benefits analysis described by the Department in Berkshire Gas D.T.E. 01-56 (2002). The Company's mixing of all promotional expenses under an IRR analysis has the potential to include poor performing and unrecoverable items. (See Intervenor Initial Brief pp. 16-17). One example is the Company's sponsorship of the San Francisco trip for selected VPI contractors. Under the Company's approach, any charges made to the promotional account will be recoverable so long as the IRR is at an acceptable level.

Additionally, MOC and the Alliance do not believe that the IRR is correctly calculated. As noted in their initial brief, the intervenors believe the 25 and 15 year terms to be too long. The intervenors also disagree with the Company's reason for excluding sales-force overhead expenses from its IRR calculation. (Company response to A.G., see Company Br. p. 90). The Company states that these are "fixed costs of the Company's operations that would not be reduced or eliminated if the Company were to terminate its marketing and incentive programs…" (Id.) In contrast, if the Company's VPI and free equipment program were curtailed or eliminated, it would appear that the level of sales personnel overhead would be reduced or eliminated. Unlike other fixed costs, these overhead costs should have been

[2] MOC and the Alliance concur with the Attorney General's analysis and position concerning the Company's promotional expenses (AG Br. pp. 49-56).

included in the Company's IRR calculations.

Under the Company's aggregate IRR approach, poor promotional programs can be covered by over-performing programs and unrecoverable expenses can be included. Intervenors do not believe that the Company has met its burden under Department precedent to demonstrate that each of these programs provide a net benefit to the ratepayers.

B. THE COMPANY'S ADVERTISING EXPENSES SHOULD BE REDUCED

The Company has misunderstood the intervenors' position with regard to allowable advertising amounts. The Company contends that MOC and the Alliance have requested that all its advertising expenses be disallowed from rate recovery (Company Br. p. 93). In contrast, the intervenors requested that all advertising costs that do not meet statutory and Department requirements be excluded from the cost of service (Intervenors' Br. pp. 5, 28).

As discussed in the intervenors' initial brief, the Department has set forth the standard of review of promotional advertising expenses and has designated certain categories in which intervenors and the Department can conduct such review (Intervenors' Br. p. 23). The Company's advertisements have not adhered to the classification specified by the Department. Boston Gas D.P.U. 96-50 pp. 63-65 (1996). The Company's approach of combining recoverable and non-recoverable advertisements makes it impossible for the intervenors to determine allowable costs. Only those expenses which meet the categorization scheme set forth by the Department should be allowed.

C. THE INTERVENORS' REQUESTED PAYBACK ANALYSIS, DISCLOSURE STATEMENT AND GUARANTEE DISCLAIMER WOULD PROVIDE CONSUMERS WITH NEEDED INFORMATION

The Company opposes the intervenors' request for a payback analysis asserting that this request has been previously rejected by the Department. (Company Br. p. 96 citing Massachusetts Oilheat Council, Inc. D.T.E. 00-57 [2001]). The utility contends the Department deferred the payback issue to other forums and that there is no reason for the Department to change its position. The Company is incorrect.

In D.T.E. 00-57, the proposed payback analysis was rejected because the Department viewed the request based on competitive grounds. The cited passage from the order specifically discusses the MOC/Alliance allegations of anti-competitive activities and refers these claims to other legal forums. (D.T.E. 00-57 pp. 9-10, fn. 6). The Department has not stated that it would refuse to require a payback analysis if necessary to protect the public interest and the potential customer.

The intervenors believe that a payback analysis, a cost disclosure statement and the suggested guarantee disclaimer would provide consumers with essential information prior to undertaking a conversion. Particularly in today's volatile energy markets, it would be in the customer's best interest to learn of potential price impacts upon the payback period before incurring the capital investment in a conversion. This is especially important where customers will be offered free equipment and rebates as incentives to convert.

The company contends that it does not know all the information necessary (i.e., cost of equipment and future price of natural gas) in order to provide such a payback analysis.

In fact, both the cost of equipment and the cost of gas are known at the time of conversion. Providing as much information as possible gives the consumer the ability to make an informed choice and does not interfere with the Company’s promotional efforts. A payback analysis, cost disclosure and disclaimer should be required.

D. THE DEPARTMENT SHOULD REQUIRE THAT THE COMPANY'S UNREGULATED HVAC AFFILIATES HAVE NAMES THAT ARE DIFFERENT FROM THE COMPANY

Initially the Company's misunderstanding of the intervenors' argument on this point must be corrected. As stated in their initial brief, MOC and the Alliance are not pursuing remedies under the Standards of Conduct for Distribution Companies and Their Affiliates (220 C.M.R. 12.00) even though some of these examples may point to violations of those standards. Instead, the examples provided illustrate the need for a change in the standards of conduct so as to restrict the competitive affiliate's use of the Company's name.[3] The intervenors are aware of the Department's reasons for narrowly defining name use proscriptions. Standards of Conduct, D.P.U./D.T.E. 97-96 (1998). However, for the reasons set forth in the initial brief, MOC and the Alliance believe a change is warranted given the pervasive name promotion under which KeySpan conducts all its business activities in the New England area.

[3] Similarly, the intervenors did not contend that the $17,000 subsidy provided through the Company's cooperative advertisement program violated the Standards of Conduct. Intervenors questioned the propriety of such a payment when KeySpan Home Energy Services, Inc. already benefits tremendously from the branding and name recognition of the Company's KeySpan name.

As noted in the initial brief, the use of a disclaimer alone, while welcomed, is insufficient to address the concern that similar company names in the unregulated market give the impression that whenever the Company advertises, it is speaking on behalf of its competitive affiliate. There is no requirement for the disclaimer other than for competitive energy affiliates. 220 C.M.R. 12.03(13). There is no disclaimer accompanying the many and varied uses of the KeySpan name and logo that is part of the overall branding strategy and promotional efforts. The affiliate's signs, letterhead, web pages, and trucks do not have disclaimers.[4]

The intervenors' proposal that KeySpan Home Energy Services, Inc. or other HVAC affiliates adopt a name and logo that do not include the KeySpan name or logo would eliminate customer confusion, and put the affiliate(s) on equal competitive footing with all other HVAC businesses in the Company's service territory.

[4] The referenced advertisement in intervenors' initial brief (Ex. AG-7) contains a disclaimer, but it is in fine print and does not eliminate customer confusion. In contrast to the Company's claim (Br. p. 97), the fact that the ad states that the Company's offer may not be combined with any other KHES offer does not distinguish the two companies. It gives the impression that they are not separate. Independent companies would honor their own offers.

III. <u>CONCLUSION</u>

For the reasons set forth above and in detail in the intervenors' initial brief, MOC and the Alliance respectfully request the recommendations they have set forth be adopted.

Respectfully submitted,

Massachusetts Oilheat Council, Inc.
and Massachusetts Alliance for Fair
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By: ________________________

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